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PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA
ENERGY DIVISION
Item 50 I.D # 2919
RESOLUTION E-3852
December 4, 2003

R E S O L U T I O N

Resolution E-3852. Pacific Gas and Electric Company (PG&E) request to reimburse the California Department of Water Resources (DWR) for payments for PG&E's renewable transitional procurement contracts on a monthly basis for actual costs incurred. Denied.

By Advice Letter 2354-E, filed on March 10, 2003.

SUMMARY

PG&E requests Commission authorization to reimburse DWR on a monthly basis for actual costs incurred by DWR for the renewable transitional procurement contracts (Interim Contracts) approved by the Commission in Resolution E-3805. This resolution denies PG&E's request, finding that PG&E is currently bound by the terms of its Operating Order and Operating Agreement with DWR for the remittance of Power Charges associated with the Interim Contracts.

BACKGROUND

PG&E filed Advice Letter (AL) 2354-E on March 10, 2003 requesting Commission authorization to reimburse DWR on a monthly basis for the actual costs incurred by DWR for the Interim Contracts approved December 19, 2002 under Resolution E-3805 (AL 2303-E).

Decision (D.) 02-08-071 authorized PG&E and Southern California Edison Company (SCE) to enter into procurement contracts with credit support provided by DWR between the effective date of the decision, August 22, 2002, and January 1, 2003. PG&E submitted several renewable procurement contracts under AL 2303-E filed on November 15, 2002, stating that until it regains its investment-grade credit rating and is able to assume all rights and obligations as specified under each contract, DWR will serve as the creditworthy purchaser for the products received. Under the decision adopting DWR's 2003 Revenue Requirement, D.02-12-045, Ordering Paragraph (OP) 14 ordered that "(a)ny DWR 2003 revenue requirement pertaining to

power contracts entered into by DWR between August 22, 2002 and January 1, 2003 (pursuant to D.02-08-071) shall be allocated to the customers of the utility entering the relevant contract.”

Resolution E-3805 states that “(u)nder the terms of the proposed contracts, DWR will be the creditworthy purchaser of the contracts and the costs of the contracts will be recovered by DWR through its remittance rate when they are included in DWR’s revenue requirement” (Res. E-3805, mimeo page 14).

NOTICE

Notice of AL 2354-E was made by publication in the Commission’s Daily Calendar. PG&E also served public, redacted copies of the advice letter to interested parties according to Section III Paragraph G, of General Order 96-A and to service list parties in docket A. 00-11-038.

PROTESTS

DWR filed a protest to AL 2354-E on April 1, 2003 and on April 25 submitted a reply to PG&E’s April 8, 2003 response to the April 1 protest. DWR argues that PG&E seeks to modify the remittance rate for DWR-delivered energy in PG&E’s service territory under contracts for which DWR currently serves as the creditworthy purchaser and that the established power charge applies to the Interim Contracts. DWR alleges that PG&E’s advice letter is procedurally flawed and, if approved, would violate applicable law and create administrative burdens on DWR. In reply to PG&E’s April 8 response, DWR submits additional arguments, citing that the relief sought by PG&E under AL 2354-E directly contradicts the PG&E-DWR Operating Agreement approved by D. 03-04-029 and executed by PG&E and DWR on April 17, 2003, and also would contravene provisions of the Operating Order applicable to PG&E adopted by D. 02-12-069, PG&E 2003 Servicing Order, Attachment B.

PG&E responded to DWR’s April 1 protest and April 25 reply on April 8 and May 2, 2003, respectively. PG&E argues that DWR is wrong in claiming that the remittance rate should be used for the power purchased under the Interim Contracts, citing that the DWR 2003 Revenue Requirement decision (D.02-12-045) did not account for these costs or for the generation supplied to PG&E ratepayers. PG&E also states that the remittance methodology in the Servicing Order cited by DWR has never been modified to address the Interim Contracts and, therefore, does not govern this issue.

DISCUSSION

PG&E's proposal to submit to DWR monthly actual costs for the Interim Contracts was made on March 10, 2003, in advance of its Operating Agreement with DWR (executed April 17, 2003), and in advance of the 2003 DWR Supplemental Revenue Requirement (submitted to the Commission on July 1, 2003, and addressed in D.03-09-018). The proposal recognized that the 2003 DWR Revenue Requirement (submitted in August 2002) did not reflect the Interim Contracts signed between August and December 2002. The proposal also recognized that the Commission had directed that the particular costs and generation associated with these contracts should be directly assigned to the utility involved (D.02-12-045). Finally, the proposal recognized Resolution E-3805 which stated that "(u)nder the terms of the proposed contracts, DWR will be the creditworthy purchaser of the contracts and the costs of the contracts will be recovered by DWR through its remittance rate when they are included in DWR's revenue requirement" (Res. E-3805, mimeo page 14).

However, PG&E also had an existing Operating Order, issued under D.02-12-069 on December 19, 2002, which recognized the Interim Contracts and, as such, obligated PG&E to "remit DWR Revenues to DWR, consistent with the Settlement Principles for Remittances and Surplus Revenues attached hereto as Exhibit C and the Servicing Arrangement" (Operating Order, Article IV, Section 4.01 (c)).

Exhibit C outlines a formula enabling the separation of generation provided by both DWR and PG&E for surplus sales and for retail sales under the combined portfolio. The percentage of DWR generation sold to retail end use customers is multiplied by the remittance rate and the resulting amount is submitted to DWR. The Operating Agreement between DWR and PG&E, executed on April 17, 2003, contains changes to Section 4.01 and Exhibit C, but these changes do not affect the outcome. No side calculation is made under either the Operating Order's or the Operating Agreement's Exhibit C to separate the allocated long-term DWR contracts from the Interim Contracts' costs and generation.

The remittance rate adopted under the 2003 DWR Revenue Requirement did not account for the generation or costs of the Interim Contracts. Applying the Exhibit C formula to this generation counts it as DWR-related generation, and the resulting percentage multiplied by the remittance rate produces an over-remittance to DWR. Using this remittance rate causes PG&E ratepayers to pay more than twice the actual costs of the generation provided under the Interim Contracts. In contrast, the Supplemental 2003 DWR revenue requirement does account for the generation and

costs of the Interim Contracts, but because these elements are not separately accounted for by DWR, all California customers pay for the PG&E Interim Contracts. No other interim contracts signed by other utilities relied on DWR as the creditworthy buyer. The annual value of the PG&E Interim Contracts is estimated to be \$53 million.

Payments and Charges

Energy Division requested PG&E to provide information on what generation and payments it has been making to DWR regarding the Interim Contracts. In a confidential response, PG&E accounts for the amounts paid to DWR from January through July 2003. PG&E's remittance has been monthly, based on the interim contract costs, not the DWR Remittance Rate. Separately, PG&E also provides confidential information requested by Energy Division, identifying DWR's inclusion of the annual generation and estimated revenue requirements resulting from the PG&E Interim Contracts in the DWR Supplemental 2003 Revenue Requirement, submitted to the Commission in July 2003. DWR did not develop a separate calculation for the PG&E Interim Contracts, and as a result, the new remittance rate for each utility now incorporates the PG&E Interim Contracts. This means that other utility retail customers are subsidizing PG&E retail customers for the Interim Contracts. Meanwhile, PG&E's customers are paying a lesser charge than would otherwise be the case. Also, if PG&E is still following its existing method of remitting monthly actual costs for the Interim Contracts, PG&E customers are also paying the actual costs of the Interim Contracts to DWR on a monthly basis.

Over Remittances

Resolving the payment issues requires adjustments affecting the Operating Order, the Operating Agreement and the DWR 2003 Revenue Requirement and the DWR 2003 Supplemental Revenue Requirement. (We clarify that the Servicing Order incorporates the Interim Contracts by reference to the Operating Order/Agreement.) An advice letter cannot resolve all the changes necessary to address the appropriate adjustments. PG&E has been forthright in its voluntary monthly payments to DWR for the Interim Contracts. It has not withheld payments for the energy provided by DWR but has submitted to DWR the actual costs incurred. PG&E has included the Interim Contract quantities in the calculation of surplus energy sales as DWR-related under the Operating Agreement so that the pro rata calculation is followed. PG&E states that it has not included these quantities in the development of the DWR percentage applied to the remittance rate for retail sales. Therefore, PG&E has followed its original payment methodology to date and has not included these DWR-related quantities in its calculations of the remittance rate for retail sales.

Given the complexity and timing of these issues, Energy Division recommends the following procedure. The PG&E remittance rate(s) must be applied to this generation to conform to the Operating Order and the Operating Agreement. PG&E should recalculate the difference between the revenues submitted to DWR and the total amount due using the remittance rates stemming from the 2003 DWR Revenue Requirement and the 2003 DWR Supplemental Revenue Requirement. PG&E should pay DWR this difference immediately, but should also track these amounts for a future adjustment in the next DWR Revenue Requirement proceeding. We have considered simplifying this approach, but believe that the over remittance can be redressed under current DWR Revenue Requirement proceedings. In its comments on the Draft Resolution, DWR recommends that late payments associated with the requirement to use the DWR 2003 Power Charge and the DWR Supplemental 2003 Power Charges be applied. Under the circumstances and based on PG&E's voluntary payment history for the Interim Contracts, we believe that late charges are unwarranted and will not order PG&E to also calculate and remit these payments to DWR.

It is not clear whether the issues surrounding these interim contracts will only apply to the 2003 calendar year, or will continue into future years. In its comments, PG&E states that it assumed credit responsibility for two of the three Interim Contracts in early November and will assume credit responsibility for the third contract in December. Therefore, DWR should not need to develop a utility-specific calculation for the Interim Contracts in a future revenue requirement determination. However, DWR should work with the parties to true up the over payments incurred under the 2003 DWR Supplemental Revenue Requirement in a future revenue requirement proceeding.

In their comments, PG&E, SCE and SDG&E submitted three different methods to correct the misallocations. DWR supported SCE's solution. We appreciate the parties' approaches to the misallocations, but believe that it is more appropriate for the parties to correct this issue through a formal proceeding. We decline under this Resolution to adjust the Power Charges for each utility stemming from the inclusion of the Interim Contracts' costs and quantities in the 2003 DWR Supplemental Revenue Requirement. PG&E, SCE and SDG&E may petition to modify D.03-09-018 to adjust their respective Power Charges so that only PG&E customers pay for the PG&E Interim Contracts. In the alternative, PG&E, SCE and SDG&E should work with DWR to true up the appropriate payments in the next DWR Revenue Requirement proceeding. In this way, all the affected parties will have an

opportunity to review and provide input to changes made to the Power Charge calculations.

COMMENTS

Public Utilities Code section 311(g)(1) provides that this resolution must be served on all parties and subject to at least 30 days public review and comment prior to a vote of the Commission. Sections 311(g)(2) and 311(g)(3) provide that this 30-day period may be reduced or waived under certain circumstances.

The 30-day comment period for the draft of this resolution was neither waived nor reduced. Accordingly, this Draft Resolution was mailed to parties for comments, and was placed on the Commission's agenda no earlier than 30 days from the day it was mailed. Comments were filed by PG&E, DWR and SCE on November 14, 2003. Reply comments were filed by DWR and SDG&E on November 19, 2003.

Payments

DWR comments that it generally supports the Draft Resolution. DWR recommends that PG&E remit interest on the difference between the total remittances PG&E owes to date for energy delivered under the Interim Contracts and remittances PG&E has made. DWR cites that the interest should be calculated at the late payment rate found in the Servicing Order adopted by D.02-12-072 (Prime rate + 3%). DWR does not believe renegotiations to the Operating Agreement are necessary since the Interim Contracts are already accounted for in the Operating Agreement. DWR is willing to separate utility-specific costs associated with the Interim Contracts in any future revenue requirement submissions, so that any future allocations by the Commission will directly assign the proper costs to the appropriate utility for purposes of establishing a power charge sufficient to satisfy retail revenue requirements as specified by DWR.

PG&E submits that although the Interim Contracts are not explicitly addressed in either the Servicing Order or the Operating Agreement, there is nothing in either document precluding PG&E from submitting to DWR the actual costs incurred under the Interim Contracts. PG&E also states that it has included the Interim Contract kilowatthours (kWhs) in its calculation of the surplus sales revenue amounts calculated under the Operating Agreement. PG&E adds that approval of its advice letter simplifies the process needed to rectify the issues addressed by the resolution. If the Draft Resolution is followed, PG&E states that DWR would be in violation of the Water Code by charging more than their costs to purchase power and argues that DWR should be compensated only for the costs incurred. To avoid

this outcome, PG&E recommends that the Commission grant AL 2354-E, and require PG&E to remit to DWR the costs DWR has incurred and is incurring under the interim contracts. PG&E argues that this is consistent with both D. 02-12-045 and D. 03-09-018, where the Commission directs that these contracts be directly assigned to PG&E.

In reply comments, DWR believes PG&E is asserting that power provided under the Interim Contracts does not constitute DWR-related power. DWR argues that the Operating Agreement explicitly provides that power and energy from the Interim Contracts constitute DWR Power as long as DWR is performing a credit-backing role for PG&E and thereby creates a direct obligation for retail customers to pay for DWR Power at the Commission established Power Charge rate. (Operating Agreement, D.03-04-029, Section 4.04) DWR also contends that contrary to PG&E's assertion that the Servicing Order does not set out the treatment for the Interim Contracts, Attachment B of the 2003 Servicing Order adopted by D. 02-12-072 provides a methodology for PG&E to remit DWR Power Charges, which include the Interim Contracts. DWR disputes PG&E's argument that DWR will over recover its costs. DWR states that its costs are subject to true up in connection with each of its revenue requirement determinations, so that DWR recovers only its costs and no more.

Misallocations

Since the DWR 2003 Supplemental Revenue Requirement (effective 9-4-03) includes the PG&E Interim Contracts and, since now SCE and SDG&E customers are also paying for them, PG&E recommends that the Commission simply remove the costs and kWh from the DWR 2003 Supplemental Revenue Requirement and recalculate the revenue requirement percentages to apply to each utility. This action coupled with approval of AL 2354-E would simplify the cost allocation and reconciliation issues.

SCE comments that the misallocation resulting from the Interim Contracts is clearly unfair to SCE and SDG&E's customers and the Commission should not allow this error to continue for the many more months it would take for the Commission to rule on a petition for modification. SCE states that "correcting or changing the incorrect Power Charges approved in D.03-09-018 is an inadvertent error or omission which does not involve a substantive change to a Commission decision", and as such, Rule 47 (j) of the Commission's Rules of Practice and Procedure can be applied to correct the misallocation. SCE states that the draft Resolution simply needs to order the affected parties to work together with Energy Division to determine the correct Power Charge for SCE and SDG&E. SCE would further require PG&E to "reimburse SCE's and SDG&E's customers "for any amounts overpaid through the

erroneous Power Charges approved in D.03-09-018 within 30 days of receipt of notification from the Executive Director of the amount PG&E owes.”

In response to SCE, DWR clarifies that it did identify the Interim Contract costs in its modeling information provided to PG&E and the Commission in a manner that would have allowed these costs to be separately allocated to PG&E. DWR does not oppose SCE’s proposed changes to the Draft Resolution.

SDG&E submitted reply comments, supporting PG&E and SCE’s recommendation that the Draft Resolution correct the 2003 DWR Revenue Requirement misallocation among the three utilities. However, SDG&E recommends that a very brief “shut-off” period be employed, as was done in D.03-09-018, allowing the misallocation to be redressed during a shorter timeframe than adjustments to the utilities’ remittance rates. The shut-off period would apply to SCE and SDG&E and would be limited to the amount of days needed for the utilities to fully recover these costs and could be implemented at any time prior to the end of 2003. Assuming the \$53 million estimate, SDG&E would use the same cost ratios used in D.03-09-018 – 13.51% for SDG&E and 42.16% for SCE – times the cost of the Interim Contracts to achieve the reallocation.

We have reviewed the comments and have made some changes to the Discussion, the Findings and the Ordering Paragraphs.

FINDINGS

1. PG&E has been paying DWR the actual monthly costs of the Interim Contracts approved under Resolution E-3805.
2. The 2003 DWR Revenue Requirement approved by D.02-12-045 did not account for the Interim Contracts.
3. Resolution E-3805 advised that when the costs of the Interim Contracts are included in DWR’s revenue requirement, DWR would recover these contract costs through the remittance rate.
4. PG&E had an Operating Order approved by D. 02-12-069, which recognized the Interim Contracts and obligated PG&E to include the generation from the contracts as DWR-related generation under the formula of Exhibit C for Surplus Sales and Remittances.

5. PG&E and DWR executed an Operating Agreement on April 17, 2003, adopted under D.03-04-029 and similar to the Operating Order, which did not materially change the formula used for determining the generation quantities applied to remittances of Power Charges.
6. The DWR 2003 Supplemental Revenue Requirement approved by D. 03-09-018 includes the PG&E Interim Contracts but allocates the costs of these contracts to all California ratepayers.
7. No other utility has executed interim contracts where DWR is the creditworthy buyer.
8. The annual estimated value of the PG&E Interim Contracts is \$53 million.
9. PG&E should pay DWR for the Interim Contract generation using the applicable remittance rate for the Power Charges established under the DWR 2003 Revenue Requirement and the DWR 2003 Supplemental Revenue Requirement.
10. PG&E should track the difference between the revenues submitted to DWR and, separately, the total amount due using the remittance rates stemming from the 2003 DWR Revenue Requirement and the 2003 DWR Supplemental Revenue Requirement for a future adjustment. Late payment interest on these amounts is not warranted.
11. PG&E, SDG&E and SCE may petition to modify D.03-09-018 to adjust their respective Power Charges adopted under D.03-09-018, so that only PG&E customers pay for the PG&E interim contracts. Alternatively, this can be addressed in the next DWR Revenue Requirement proceeding.
12. PG&E, SCE and SDG&E should work with DWR to true up any appropriate payments for the Interim Contracts in the next DWR Revenue Requirement proceeding.
13. PG&E's request under Advice Letter 2354-E should be denied.

THEREFORE IT IS ORDERED THAT:

1. Pacific Gas and Electric Company shall recalculate the total revenues due to the Department of Water Resources for the Interim Contracts using the remittance rate for the Power Charges adopted under the 2003 Revenue Requirement and the 2003

Supplemental Revenue Requirement, shall deduct from this an amount equal to what has been paid, and shall remit the difference to DWR immediately. Late payment interest shall not apply.

2. Pacific Gas and Electric Company shall continue to count the power from the Interim Contracts as DWR-related power and shall apply the resulting percentage to remittance rate for Power Charges until DWR relinquishes the contracts to PG&E.
3. Pacific Gas and Electric Company Advice Letter 2354-E is denied.
4. This Resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed and adopted at a conference of the Public Utilities Commission of the State of California held on December 4, 2003, the following Commissioners voting favorably thereon:

WILLIAM AHERN
Executive Director